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**Godrej Consumer Products Limited
Q2FY12 Conference Call Transcript
11.00 am, Saturday, October 22, 2011**

Moderator: Ladies and gentlemen good morning and welcome to the Q2FY12 results call of Godrej Consumer Products Limited hosted by Emkay Global Financial Services. We have with us today Mr. Adi Godrej, Chairman and the Senior Management Team. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. If you should need any assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Pritesh Chheda -- Senior Research Analyst of Emkay Global. Thank you and over to you Mr. Chheda.

Pritesh Chheda: Good morning and thank you for joining us today. We would like to welcome the management of Godrej Consumer Products Limited and thank them for giving us the opportunity to host his call. We have with us Mr. Adi Godrej, Chairman and the senior management team of Godrej Consumer Products Limited. I would now like to hand over the call to Mr. Adi Godrej for the opening remarks. Over to you, Sir

Adi Godrej: Thank you Pritesh and good morning everyone. I welcome all of you to the Godrej Consumer Products Limited conference call for the Second quarter of financial year 2012. Joining me today on this conference call are Mr. Mahendran, Managing Director, Ms. Nisaba Godrej, Director and President, Human Capital & Innovation of the Godrej Group, Vivek Gambhir, Chief Strategy Officer, and P. Ganesh, Executive Vice President – Finance & Commercial and Company Secretary.

We will begin with an update on our six key business imperatives and how we have performed on these priorities. After this, I will discuss the highlights of our financial performance during the quarter.



One of our most important imperatives was to sustain leading positions in the three core categories that we participate in – Home Care, Hair Care and Personal Wash. Across these categories, our focus is on growing ahead of the market, driving consumption and penetration and strengthening our portfolio. If we look at our domestic business, across categories, this has been one of the strongest quarters for sales growth in the recent past.

Our household insecticide category delivered yet another quarter of robust performance, with a 29% sales growth, at more than twice the pace of category growth. We are reaping the benefits of strong marketing and promotional initiatives. We continue to gain market share and enjoy leadership positions across all formats of electrics, coils and aerosols. Our focus on innovation and the synergistic distribution opportunities from the GCPL-GHPL merger are enabling us to make continued gains in this category.

Our Soaps business grew by a stellar 32% for the quarter, with a volume growth of 19%, way ahead of the flat category volume growth. This is the third consecutive quarter of strong sales growth. We continue to be the second largest toilet soap player in the country. Our performance across both our key brands - Godrej No.1 and Cinthol was very strong. The response to our newly launched Godrej No.1 Saffron and milk cream variant has been very encouraging. The success of our new launches and re-launches, along with our intensifying marketing and promotion focus, has contributed to this strong growth momentum. Gross margins for the category have expanded sequentially with full impact of price increase and sequential drop in oil prices. We will be diligent about trying to protect our margins along with gaining volume market share through efficient sourcing of oil, prudent cost management and calibrated price increases.

We continue to enjoy market leadership position in the hair colorant category, which continues to do well and grew by 15% during the quarter. Our recent launches, Expert Care – a herbal based formulation and Expert Advanced – a progel formulation, have received very positive response. We expect to see further momentum in this category as these new launches gain further traction in the market.

The second pillar of our strategy was to drive growth in our international business, guided by our 3x3 framework, of being in three core categories and in emerging geographies in Asia, Africa and Latin America.



Our biggest international business, Megasari in Indonesia continues to grow at a strong pace. This is the first quarter of the comparable base and the business had a strong sales growth of 27%. Megasari is the market leader for aerosol household insecticides, air care and wipes in the Indonesian market. EBITDA margins were at 19.4%, which expanded both sequentially and year over year basis behind favorable category mix, healthy performance of new launches and prudent cost management. We continue to focus on innovation and launched Stella bathroom and Stella Car air freshners and Mitu Milk bath during the quarter. HIT Magic, a disruptive innovative paper format mosquito repellent, launched last quarter, continues to penetrate into the coils market and is being backed by very strong marketing investments. We are very excited about the HIT Magic developments and their global implications and applicability.

Our African operations, which comprise Rapidol, Kinky, Tura and Darling, made steady progress during the quarter. Revenues grew by 47%, clocking EBITDA margin of around 26%. Rapidol continues to grow strongly at 28% during the quarter behind expansion in distribution reach and entering newer geographies. Kinky will synergize on go to market and backward integration facilities of Darling South Africa operations. We expect stronger sales growths and expansion in Kinky margins from integration synergies commencing from quarter four of this fiscal year. In Sep 2011, we closed the Nigeria and South Africa parts of the Darling transaction. We have also begun a rigorous, but selective process of integration in key areas of the business. In October 2011, we completed the Mozambique leg of Darling group acquisition. We have also begun rigorous work on phase 2 of the Darling group acquisition.

Our Latin American business, the Issue Group and Argencos reported sales growth of around 13% with EBITDA margins of around 7.4%, which has expanded sequentially as well as on a year-over-year basis. We continue to invest in growing our business in the neighboring countries of Argentina. The initial response to the Ammonia-Free Issue hair color which was launched last quarter has been very positive. This continues to receive strong marketing investments. We launched Diamond Black hair color cream in kits, flowpack and sachet formats, Roby Glam & Gloss hair serum, the solution for dry and split ends and the Roby Glam and Gloss hair gloss which gives an instant shine that stays for hours.



Our UK business registered good revenue growth of 10%, with EBITDA margin at around 11%. Brands like Bio-oil, Cuticura and Touch of silver continue to grow well. This is our second running quarter of strong growths and we are optimistic about growth opportunities going ahead.

Our third strategic pillar was to accelerate the pace of innovation and to strengthen our brand portfolio. In this fiscal year, we have launched multiple innovative products across categories both in our domestic and international business. In domestic markets, we took a first step towards premiumization in the hair colour category, with launch of Expert care – a herbal based formulation and Expert advanced – a progel formulation with triple conditioners. We launched a new variant of Godrej No.1, the saffron and milk cream soap. Internationally, we launched HIT Magic paper, Stella bathroom and car air fresheners, Mitu milk bath in Indonesia, and range of hair care products in Latin America.

We will continue to step up our innovation intensity across categories both in domestic and international markets. These new launches will be backed with adequate marketing investments. We believe that we have a robust innovation pipeline across categories. Our focus on innovation and brand building has resulted in Goodknight, Cinthol and Godrej No.1 featuring in ET's 100 most trusted brands survey.

One of our other key imperatives was creating a future ready sales organization for domestic business. We have been able to leverage our scale, expand urban coverage and tap rural potential especially for the household insecticide category. We have also adopted best in class sales processes and practices. We will also continue to explore newer and untapped sales channels.

Our fifth pillar was to create a global and best in class supply chain. We have taken strong steps in this area by establishing centers of excellence in TPM, lean, six sigma and low cost automation. We have also set up a strategic sourcing team to leverage scale and reduce our procurement costs.

Our final imperative relates to fostering an agile and professional entrepreneurial culture. We were recently ranked by Hewitt as the number one FMCG Company to work for. We have recently conducted an extensive engagement survey across both domestic and international businesses to assess how to build a higher degree of engagement with



employees. In the domestic business, to harness the benefits of scale and scope from the GCPL-GHPL merger, we continue to streamline our operations and make our organization structure more effective.

Before I provide an assessment of our financial performance, I would like to spend a few minutes on the evolving global currency situation, our foreign currency exposures and any potential impact. To begin with, we have a forex committee that closely monitors all exposures and takes calls on hedging exposures. We covered our near term exposure on oil payables till December 2011, well before the INR depreciation started in August. As on 30th Sep 2011, we had import exposure of US\$22 million. The earliest exposure is falling due in Jan12. This exposure has resulted in a mark to market impact of Rs 11 crore in the standalone financials.

The net exposure is US\$13 million and impact in the standalone financials after revaluation of export receivables is Rs. 8.5 crores. There is a mark to market impact of Rs 8 crore in our overseas subsidiaries on account of revaluation of intercompany loans. These are long term loans and hence mark to market impact will reverse as and when the currencies appreciate. The total mark to market impact at consolidated level aggregates to Rs 16.5 crore. As you will appreciate, the global environment continues to be uncertain. As always, we will continue to closely monitor the situation and take actions to limit any adverse impact from current fluctuations, as necessary.

For the quarter ended September 30, 2011, our consolidated net sales stood at Rs. 1186 crore, growth of 23%. EBITDA margins strengthened to 18.1% with a growth of 24% and expansion of around 320 basis points sequentially. Earnings per share non-annualized stood at Rs. 4.0 for the quarter. The Board of Directors have declared a second interim dividend of 100%, which translates to Re. 1 per share. Both our domestic and international businesses have performed well. Our net sales in the Indian sub-continent increased by 24% to Rs. 776 crore, with significant growth across all our three core categories. EBITDA margins strengthened to 19.2%, with a growth of 9% and sequential expansion of around 250 basis points. Our international operations, which accounted for 35% of our consolidated turnover during the quarter, reported revenues of Rs. 419 crore, a growth of 24% and a like to like growth of around 19%. EBITDA margins strengthened to 15.8% with a growth of 72% and sequential expansion of around 400 basis points. I am confident of the opportunities ahead for GCPL, both in India and overseas. In the coming quarters we



expect to have a favorable category mix, being the season for liquid detergent and household insecticide. Higher sales and cost synergies are also expected to kick in arising out of domestic business integration. Internationally our Africa and Latam business are expected to clock strong sales on the back of festive season and synergies in hair extension category. All of this should result in stronger operational growth and healthy margins. Also, any positive currency movements from September levels will result in higher profits.

The macroeconomic environment continues to be challenging and I believe that our strong operating performance is a reflection of a robust business model, a great team and our ability to manage risks and challenges efficiently. On all operating parameters, our business continues to hold strong ground. In these uncertain times, our approach will remain to be close to our consumers, to respond to their needs, to strengthen our brands, to accelerate our innovation pipeline, and to invest in our talent. We will focus on execute strong execution in the near term while positioning ourselves for even greater successes in the longer term. We will continue to pursue a prudent but aggressive growth strategy, through a blend of organic and inorganic initiatives. As always, we will strive to enhance shareholder value and drive growth. I now conclude my opening remarks and open the floor for questions.

Moderator: We will now begin with the question-and-answer session. We have the first question from the line of Percy Panthaki from Daiwa, thank you and go ahead.

Percy Panthaki: My question is on the working capital front; you have mentioned that your working capital has come down not only as a percentage of sales but in absolute value as well. So just wanted to ask how this happened and secondly is this cyclical in nature or is this sort of a sustainable trend in terms of percentage of sales, shall we take it at a lower level going ahead?

P Ganesh: When we look at working capital both in India as well as our overseas geographies, we have been consciously working on streamlining things, optimizing working capital requirements, etc. So it's a conscious effort which has gone into this and also in situations where we are looking at possible tightening of liquidity, etc, it always helps to be more prudent and optimize working capital. So it's very much a conscious effort and we should see sustaining or improving these levels going forward as well.



- Adi Godrej:** I would just like to add that in India we work on negative working capital. We have several techniques we use to keep working capital under control. In international markets of course with larger percentages of business going to modern trade, I don't think we would be able to get into negative working capital situation, but we bring in our learnings from India into the acquired companies and try and reduce the working capital very considerably.
- Percy Panthaki:** Will you be able to elaborate for the international business, if the reduction has happened in any particular geography or it has happened across the board? And secondly which item of working capital has led to this reduction, is it debtor, inventory or creditors?
- P Ganesh:** It's largely on debtors and creditors and it's happened largely across our various geographies.
- Percy Panthaki:** On the domestic business, where basically we have seen category such as Soaps, has grown very well. Why is it that this has grown so well? Obviously, it is all on account of your innovation efforts and other initiatives on your part. But if I remember correctly Godrej No 1 has always followed a variant strategy and always has come out with new exciting products. So why is it that only in this particular quarter, we have seen such a large impact? And secondly, I also noticed for your domestic business that your promotional spends have gone up quite sharply, so is it a result of the promotional spends and is there any concern you have that you might hear repeat of what had happened one and a half, two years back when your pipeline had expanded and then sales were effected in subsequent quarters?
- Adi Godrej:** A lot of our great success on sales increase is due to the synergistic benefits being received from the merging of the two businesses and that has helped us in all our categories, especially in Household Insecticides and the Soap business.
- A. Mahendran:** Apart from the synergistic benefit of the two companies merger, on distribution, in this quarter, we started tracking well on the rural side because we have embarked on a specific program for the rural penetrations of soaps also, so that has helped us during this quarter. And I just wanted to touch base on your concern which you were talking about referring to the previous year. We have an absolute control of the distributors stock level and in the model what we are operating now very strictly is a replenishment model for all the distributors who have the stock. So the question of giving extra stock more than the prescribed number of days of stock holding of distributors does not arise. So this robust



system also helps to maintain the distribution hygiene very well. So on the price part, the wholesale market is very reasonably under control across the region. Overall, there is a healthy scenario at distribution front, so that also enabled us to deliver better performance. We have done good creative investment on advertisement for that and the copy and the creative input during that first quarter is definitely tracking well in the second quarter also.

Percy Panthaki: On the Africa business, you have mentioned that growth rate is 47%. Can you tell me what the organic growth rate in Africa is? And secondly, can you also tell me in terms of MTM losses, what do you see going ahead in the next quarter or the quarter after that?

Adi Godrej: Rapidol growth was 28%, so clearly the 47% includes the new addition of Darling. On the MTM question, it's very difficult to predict how the currencies will move. As you know, it will depend a lot on how the global situation evolves. By November 3rd, we will have a clearer picture of how the European situation evolves. We have to also see how the Reserve Bank responds to the depreciation of the Indian rupee. There has been a strong voice from almost all parts of Indian business that the Reserve Bank should ensure that the rupee does not depreciate very considerably. It's difficult for us to predict how it will move. But all I can say is that if the rupee recovers as it did in 2010 from the depreciation in 2009, then the mark-to-market will also by and large get reversed. And it's not just the Indian rupee; it's also to do with the Indonesian Rupiah.

P Ganesh: I would also like to add that the mark-to-market which you are seeing coming from the international operations is purely notional because this is arising on account of shareholder loan given by the holding company to the subsidiary companies in LATAM and in Indonesia. These being essentially shareholder long-term loans, as and when the currencies appreciate back this gets reversed, so it's purely notional.

Percy Panthaki: But doesn't this get knocked off at consolidation?

P Ganesh: It doesn't get knocked off at consolidation level because this is being given from a holding company at a level lower than India and not from GCPL.

Moderator: Our next question is from the line of Abneesh Roy from Edelweiss.



Abneesh Roy: My question is more on the domestic side. Could you tell us on the Soaps business, Hair Color business, and HI, how have we done versus the competition and some insight on the rural versus urban and some insight on the market share?

Adi Godrej: In Household Insecticides and Soap, we have grown much ahead of the category growth. In Hair Color we have grown a little lower than the category growth. Market shares are difficult to judge because we find AC Nielsen figures are difficult to be definitive about, but we have provided both category growth and our growth. So in soap, the category growth is 10% and our growth has been 32%. Category volume growth has been flat to negative 2% and we have grown 19%. In Hair Colors, we have grown 15%, that's little behind the category growth which was in the low-20s and in Household Insecticides; the category growth as shown by ACNielsen was 10%. It might have been a little higher actually, but our growth was 29%.

Abneesh Roy: Sir coming to Hair Color, which is the only segment in which we have grown slightly slower, do you think it's a problem with the Nielsen data as usual or is there something more to it?

Adi Godrej: There is tremendous competition in the Hair Color business. As we launch new products, the competitors also got very active. So we are looking at various new innovations to be launched. We are very confident that we will recover the Hair Color growth to a smarter number. It's difficult for us to tell whether the Nielsen figures for the category as a whole are accurate or not.

A. Mahendran: I just want to add, in Hair Color, when we talk about category growth, there is an issue in terms of reporting by ACNielsen, of grouping what is hair color, particularly, the Mehendi type as well as the unorganized players, they have grouped into that, Lot of small players are also there. But if you strictly look into our Powder Hair Color variant, which we are focusing on as our mainstay, it is not that we are behind, but ACNielsen doesn't give the category growth of that specific variant, so it's a grouping issue.

Abneesh Roy: And sir on the higher competition, which are these key players, which have kind of ramped up more may be in non-powder?

Adi Godrej: Across the board we saw greater advertising in this category, whereas in other categories we have seen little reduced advertising.



- Vivek Gambhir:** We launched our new expert range a couple of quarters ago and typically in the hair coloring category given purchase cycles, it takes about 2 or 3 quarters for us to see full results from the innovation. All the indicators that we track internally on an operating level suggest very positive response to the new launches, but I think you would see a lot more traction in the following two quarters hopefully from these launches.
- Abneesh Roy:** In the Soaps business, numbers have been a bit volatile especially between your growth and may be industry growth, and your own growth say on a consistent basis. So, I want to understand why we are seeing this divergence, is there any one-off, is it because of the low base? What's the growth you expect on a consistent basis?
- Adi Godrej:** It's not a one-off thing; we have been growing very consistently over the last three quarters. The quarterly growth in the last three quarters has been 17%, 19% and 32% in the September quarter. So we have been doing very well in our soap business. Our market hygiene is excellent. So we think it is all going to the consumers very strongly and I think overall, it should reflect on our long-term shares and brand building in Soap.
- Abneesh Roy:** And on the rural versus urban front, are you seeing any kinds of a slowdown in the high growth rural market, any consumer sentiments impacting growth for your segment?
- A. Mahendran:** On the soap segment, we are not seeing any slowdown, at least for the Q2 on the rural side at all. As far as we are concerned, we have embarked on a lot of rural initiative in the last two quarters particularly. So that is factoring well for us, but overall if, there is no indication of slowdown in the rural side for us on the Soaps segment.
- Abneesh Roy:** And for the other two segments?
- A. Mahendran:** In all the segments we are not seeing a slowdown
- Adi Godrej:** I think generally Household Insecticides are under penetrated in rural India and I think our Household Insecticides rural business is definitely benefiting from our strong rural presence in the Soaps and Hair Color business.
- Abneesh Roy:** Sir, my second question is on the margin front. We have seen palm oil prices now at the YTD low, not may be YOY low, but taking into account, the rupee impact, are we seeing



much better gross margins quarter-on-quarter and where do you see pricing action? In the past you have maintained price cuts don't happen in any FMCG, so some color on that?

Adi Godrej: The costs of vegetable oils are quite high and our soap margins are lower than they should be. That is one of the reasons for YoY drop in standalone margins. Normally, our profit growth is ahead of our sales growth and we are very clear, the industry will need further price increases in the Soap category. We don't see if the global economy and if Europe take steps to see that they are stable, we feel vegetable oil prices may go up again and therefore we are in favor of further price increase in the Soap business and we feel our competitors seem to be so too.

Abneesh Roy: And sir has this adverse movement of rupee impacted the raw material scenario in Soaps higher?

Adi Godrej: Yes it has, other things being equal, if it's a long-term phenomenon, it definitely would, if it correct itself, then we don't do much of it. Mark-to-market could get reversed.

Abneesh Roy: But rupee does not impact the other two segments that much in the domestic side?

Adi Godrej: Not much.

Abneesh Roy: On the advertising side, in India, how do you see the trend for the three segments? We are seeing slowdown for the broadcasting companies which have reported numbers, so does that benefit us or we would continue to remain at the higher side?

Adi Godrej: As you would have noticed in the first quarter, we invested much more in advertising than the corresponding quarter of the previous year because we had also received Kiwi settlement charges etc. In the second quarter also our A&P expenditure was higher, even internationally; we are spending much more on advertising than we did in the previous year. So clearly, we expect advertising expenditure to go up. It would be moderated based on competitive situations.

Abneesh Roy: What is the guidance on tax rate? Earlier tax rate, I think consol business guidance was around 23%, what is the guidance now?



- Adi Godrej:** It is expected to be 23% over the year. Quarter to quarter, it depends on which companies have higher profit, which has lower profits, even if you take it this quarter, consolidated tax was about 24.8% but overall even for half year, it is around 23% and overall for the year, expected to be around 23%.
- Moderator:** Our next question is from the line of Nillai Shah from Morgan Stanley.
- Nillai Shah:** Sir, in the Africa margins, the 26% margin is something I have not quite understood; could you help me with that?
- Adi Godrej:** Yes, we had consolidated Darling numbers for one month and there is an issue there on the sales mix. So I don't think this is something that is going to continue. Darling margins will be higher than other margins. Also, we expect Kinky margins, which have been under pressure will improve dramatically once the Kinky business and the Darling business is operationally merged by the fourth quarter. So we expect African margins to improve, but we should not take this quarter's margin as an explanation for what the future margins will be. Sales mix was very odd when we took over that business in Nigeria especially.
- Nillai Shah:** The second thing is Indonesia margins, what is the margins post the payment of royalty and the technical fee, etc.?
- Adi Godrej:** 17% and y-o-y expansion of about 50-60 basis points.
- Nillai Shah:** In terms of the numbers on pre and post the technical fee, why the 200 basis points has gone to 50 basis points?
- P Ganesh:** See essentially it's only a notional one because it's a payment of a royalty, technical fee from Indonesia into India. So the right way of looking at this is in terms of gross margin, and gross EBITDA margin for the business was about 19%-odd during the quarter.
- Nillai Shah:** All the money paid for Darling seems to have gone to goodwill on consolidation, so is it a fully depreciated asset which you have picked up?
- P Ganesh:** No, typically if you look at any of our businesses, FMCG essentially has only working capital as an asset on the books, because most of the value paid is for the brands. So most



of that will be in value not just for Darling, but even for all our other acquisitions comes in the form of goodwill.

Nillai Shah: But over year, it seems to be 100%, is that true?

P Ganesh: No, it's not 100%, but it's a very substantial part.

Nillai Shah: Okay and the last question is on the working capital, I didn't quite understand the reduction because I am seeing an increase in the networking capital, the reduction is coming only once you take into effect cash on the book?

P Ganesh: Yes, when you look at working capital, you should look at it net of cash, on gross basis, yes, you are right, including cash because cash balances are significant, but when you look at net of cash, there is a reduction.

Moderator: Our next question is from the line of Sundar S. from Spark Capital.

Sundar S.: Sir, if you could split the international number, I think we have 23% sales in international, can we have a split in form of the organic growth, the currency, and the acquisition, is that possible sir?

Adi Godrej: 19% was the organic growth in the international business and 17% without the currency factor.

Sundar S.: Sir could you explain something on the LATAM business, we see high inflation breaking up in the LATAM business, we see a 13% growth, what contributes to volume and what contributes to pricing, if that's possible?

P Ganesh: The real growth at LATAM is about 20%, after factoring in currency, it comes to 13%.

Sundar S.: Sir, we hear that governments in LATAM have posed certain curbs on not increasing prices, how far is that true sir to curb inflation?

Adi Godrej: It doesn't affect that much.

Sundar S.: Okay sir and you are talking about the synergies between GCPL and GHPL. What kind of synergies are we talking here?



- P Ganesh:** Distribution led synergies resulting in stronger sales growth
- Moderator:** Our next question is from the line Himani Singh from Elara Capital.
- Himani Singh:** Sir, first my question is on the Soap category. As you said that we are reaping in benefits of distribution from the GHPL-GCPL merger, could you please elaborate, are we entering into newer areas or have we increased the distribution reach, and if that is so, what is our future target in terms of distribution?
- Adi Godrej:** As we are merging the two operations, we are generating synergistic benefits of one from the other. So for example, our Household Insecticides business is extremely strong in southern India. GCPL is very strong in northern India. And as we merge the two distribution channels, one takes advantage of the strength in the other geography. GCPL is very strong in rural India. Household insecticides category and erstwhile GHPL are not therefore very strong in rural area. Now, we are synergizing the rural benefits of GCPL. We are very strong in the Chemist sector in Godrej Household Insecticides business, because the nature of that. We are synergizing our GCPL distribution with that. So overall, both the categories are benefiting from this combined distribution synergies.
- A. Mahendran** Just to add to Mr. Godrej, one more point is that deployment of talents, all well trained people, post-merger of both the companies in the rural India has given us good benefits
- Himani Singh:** Sir, could you do a break up of rural versus urban in the Soap and Household Insecticides category?
- Adi Godrej:** It is very difficult to define because to be quite frank, sales made in urban areas can go to rural areas through wholesaler. But generally, we feel roughly about 35% of our sales come from rural India.
- Himani Singh:** And sir since you said that we are cross synergizing the chemist and the rural benefit of HI and GCPL and vis-à-vis, is it good to assume that going ahead, our promotional expenditures will remain high at least for this second half?
- Adi Godrej:** That in turn is determined by competitive situations, new products, innovations, etc. so it is very difficult to tell. But since our profits to-date are running at 44% profit after tax over the previous year we have a very good year going ahead. We are tending to invest more



into developing our brands and sales for the future. So I think by and large we will end up with a considerably higher advertising and promotion expenditure for the year compare to the previous year.

Himani Singh: And sir, my last question is regarding the Indonesian Megasari business. It has reported a 27% growth, could you elaborate how much would be volume and value and what is driving this strong growth?

Adi Godrej: I think it's mainly volume and particularly our new Hit Magic paper which to us is path breaking new development. Currently, it is only in Indonesia, but we hope to introduce into many other geographies including India. So that has helped us tremendously in the Indonesian sales growth, but generally Indonesia has done well both as an economy, country and our business particularly has done very well.

P Ganesh: I would also like to add that the 27% growth is in rupee term, the local currency growth is about 20%.

Moderator: Our next question is from the line of Amnish Agarwal from Motilal Oswal.

Amnish Agarwal: Sir, my first question is regarding the currency movements. You said that in LATAM, the sales growth net of currency that is in local currencies, 20% and the same number is for Indonesia. So if we have to look at the entire international business, what could be the organic sales growth in the local currency terms and what could be the organic EBITDA growth in local currency terms?

Adi Godrej: That is a difficult number to arrive at because you can't compare say the Argentinian Peso with the Indonesian Rupiah. We think if we take currency fluctuations out and we take acquisitions out, our growth has been around 17%.

Amnish Agarwal: Sir secondly if we look at many of our subsidiaries and many of our business units, we have done a host of new product launches. And my understanding is that whenever any company launches new products, a lot of inventory goes into a system. So what could be the element, of say the first time your inventory which goes into a system when the company launches a product, in your current sales growth?



- Adi Godrej:** I would like to differ from your assessment. Because even when we have new products there might be some stocks going into the system, but we monitor the total stock in the system in terms of number of days and the number of days of stock with our distributor is lower than at the beginning of the quarter.
- Amnish Agarwal:** We have gross debt of around 2,500 crore, which is I think purely foreign currency debt and which is unhedged, so any change in the strategy of the company on hedging this because say if the rupee stays at around the level it is and it was only a notional loss of around 250 crore in the balance sheet?
- Adi Godrej:** If you remember a very similar situation, when there was a global slowdown in 2009, a similar situation developed where the rupee depreciated, but within a few months, the rupee started appreciating again and ended up pretty close to 44 or 45 after appreciation.
- P Ganesh:** And also these loans are very long-term loans with end maturities of 5 to 6 years.
- Amnish Agarwal:** Okay so are we taking a view that in the next 5-6 years Rupee-Dollar will remain at the level it is?
- Adi Godrej:** I would say we take a view from time-to-time, however, hedging does not solve the problem, because there is a forward premium.
- Moderator:** Our next question is from the line of Prakash Kapadia from Alfa Investments.
- Prakash Kapadia:** If you can elaborate the details of the other expenditure, it has gone up substantially on year-on-year as well as on a sequential basis, it stands at around 18.2%. So to which head was that other expenditure? Because some of the startup cost, the legal cost would have been incurred. And if you could throw some light on the advertising expenditure, which we can expect over the next two-three quarters?
- P Ganesh:** The other expenditure, essentially, is a mix of various item heads which are largely sales spends, utility cost, processing charges, freight, selling and distribution expenses, also we need to factor that we have a category mix change where there is a significant amount of Household Insecticides in terms of sales, but this is largely led by high traction of sales growth as well as higher production.



- Prakash Kapadia:** So it's more of sales promotion expenditure, is that?
- Vivek Gambhir:** It's a mix of various expenses, also when you look at within the category, something like Hair Color has slightly lower promotion as compared to Household Insecticides, so category mix also plays a role.
- Prakash Kapadia:** Sir, if I see the advertising and the sales promotion expenditure for the consolidated basis over the last five to six years, it has been at an average of 10.8% advertising and sales promotion put together, so is that a fair number to expect or has that increased?
- Adi Godrej:** It can fluctuate depending on the market situation, but it's a fair number.
- Prakash Kapadia:** And some sense if you could give us on the advertising?
- Adi Godrej:** That entirely depends on the competitive situation, market potential, etc. but it is very difficult to predict, but generally, we have seen over the last few quarters, our advertising expenditure has been increasing.
- Prakash Kapadia:** We have seen a gross margin improvement. So is it then fair to say the ad spend has been cut and we have spent more on sales promotion, and that is why partly we see that in other expenditure
- Adi Godrej:** Even my advertising expenditure has increased. What you see under advertisement is entirely advertising.
- Prakash Kapadia:** Right, so on a comparable basis, it was 10.2% last year, it was 11.7% in Q1 and for the current quarter, it stands at 9.3% that's percentage of the sales.
- Adi Godrej:** It's very difficult to predict this percentage exact, last year Q1 spends were also higher because we had new launches during the quarter.
- Sameer Shah:** Also if you look at sequential spends in terms of absolute value, the spends have been same. I think it is only driven by the strong sales growth which we had in Q2, the percentage has gone down.
- Moderator:** We have a question from the line of Vivek Maheshwari from CLSA India.



- Vivek Maheshwari:** One question on advertising in domestic business, this quarter we had around less than 7.5% A&P which is down both yoy as well as on a sequential basis. Are you suggesting that in the second half, the A&P would go up to average at around 10% for the full year?
- Adi Godrej:** We don't look at advertising expenditure as a percentage of sale, we look at absolute advertising expenditure. If the sales growth is very strong, we don't necessarily have to advertise more. In fact it is the opposite effect. So internally, we look at advertising as an absolute expenditure, not necessarily as a ratio to sales.
- Vivek Maheshwari:** On the gross margin front in the first quarter, assuming the mix is the same this year versus last year, the gross margin contraction previous quarter was 150 basis points and in this quarter it was 300 basis points. So if the mix is moving in favor of Household Insecticides, the decline should have been lower. Is it largely attributable only to Soap?
- Sameer Shah:** Two things over here. Actually if you look at the category mix change, the Soaps growth has been 32% and HI growth has been 29% with Hair Color is 15% and on a year-over-year basis, there has been a drop in gross margins of Soaps. One other point is actually if you look at consolidated level, our gross margins have expanded year-over-year basis.
- Vivek Maheshwari:** Of the 2500 crore debt that you carry, how much would be the foreign currency part, is it still \$350 million or its higher now?
- P Ganesh:** No, the rupee debt is closer to about Rs 250 crore, balance is all in US dollar denominated.
- Vivek Maheshwari:** And the repayment will be 5 to 6 years from now, right?
- P Ganesh:** Yes it is a repayment over a 5 to 6 years period.
- Vivek Maheshwari:** And just one small bit on minority, is that mainly because of Darling and that's something that will continue, right?
- P Ganesh:** That's right.
- Moderator:** We have next question from the line of Miyush Gandhi from SBI Life Insurance
- Miyush Gandhi:** I just wanted to understand our goodwill has gone up by close to 500 crores. So can we equate this to the acquisition of Darling?



- P Ganesh:** It's largely on account of acquisition of Darling and part of it is also on account of the fact that the rupee has actually depreciated versus US dollar. So that's also revaluation impact coming in.
- Miyush Gandhi:** Okay, so that impact has directly been taken to the balance sheet?
- P Ganesh:** That's right.
- Miyush Gandhi:** And in terms of paying for the acquisition, have you already paid or we still have to pay for it?
- P Ganesh:** Yes, this has been fully financed by debt.
- Miyush Gandhi:** Okay so in terms of the balance, we will continue with this kind of 2,500 crore of gross debt and 400-500 crore of cash?
- P Ganesh:** Cash, some of it would get utilized for loan repayments, but when you look at the debt, that's the current level of debt which would by and large remain except for repayment which happens over a period of time. And on an average, the debt repayment would be in the range of 400 to 500 crore per year.
- Miyush Gandhi:** Okay and because recently you were in the market for raising debt as well, so we were wondering, what is the strategy in terms of managing the balance sheet?
- P Ganesh:** It was not a fresh debt; it was a rollover of an existing debt.
- Moderator:** Our next question would be from the line of Aashish Urganlwar from Spark Capital. Thank you and go ahead.
- Aashish Urganlwar:** Just wanted to know what the kind of volume growth is. The total revenue growth in case of Household Insecticides in India and also in Hair Color
- Sameer Shah:** If you look at Household Insecticides, the growth has been predominantly volume-driven, so out of 29% growth, 90% plus of it would be volume led. In case of Hair Color, 50% would be volume led and 50% would be price increase led.



- Aashish Upganlwar:** And about the new launches could you just shed more light on the new launches across international as well as domestic businesses, how do you see them trending because we have heard a lot about the HIT Magic paper being successful and there are certain launches in Stella which are doing pretty well. So just some more insight into how you are looking at the market taking these launches and a progress in these categories forward?
- A. Mahendran:** As far as the new launches in Indonesia, Hit Magic, it has already picked up about 10% of the coil market there in terms of consumption. Stella has also moved forward and we are looking at some new product launches in Argentina also and as well India. So overall to answer your question is that all our initiatives and innovations are doing well and we are expecting that to do well in the next coming quarters also
- Aashish Upganlwar:** Okay and how about the the LATAM market? We have not seen good numbers coming for the last two quarters, so how do you see that going forward, is it going to be an improvement from these kinds of numbers or is it looking a bit difficult compared to Megasari we have?
- Adi Godrej:** LATAM growth is good but when it is translated into rupees, it comes down because of the currency fluctuations.
- P Ganesh:** Also there is a seasonality impact, where the period closer to Christmas is actually the season period for LATAM.
- Aashish Upganlwar:** And any comments on the margins in LATAM? These are pretty low compared to what we have been expecting?
- Adi Godrej:** We are spending a lot of money on promotion for the new products, because there is huge opportunity.
- Vivek Gambhir:** I think having said that margins in Latin America will be lower than India. We have always expected that but I think the future trajectory is quite robust. We have launched a very disruptive ammonia free - hair coloring cream, we have launched some hair serums, and I think the next quarter is typically the busiest quarter for Latin America with the festive season. So you will see hopefully both improvements in top-line and bottom-line over the next two quarters.



- Adi Godrej:** And these are also the summer months in LATAM.
- Vivek Gambhir:** The other important point you mention is that as part of our strategy we are using Argentina as a platform to expand our presence in neighboring geographies, Uruguay, Paraguay, Peru, Chile, Colombia are some of our priority geographies. So some of this is in investment mode to actually lay the footprint out which is again part of our strategy and so longer-term I think that's the right call to make to establish a broader Latin America presence using that platform.
- Aashish Uppanlawar:** But how far have we been successful in exploring these markets, will it be a slow drawn process where we are going to see the effect on the business overall considering the size that we have in Argentina to be may be a two-three years period, where we can see a gradual improvement coming in?
- P. Ganesh:** It's a phased approach. Currently, about 20% of our revenues come in from ex Argentina markets in Latin America, we are hoping to continue building on that over the next one or two years.
- Aashish Uppanlawar:** Sir on the forex bit, we had about 16 crore number that has come in the P&L, so we should not expect much of movement on this side. Most of it has gone into the balance sheet.
- Adi Godrej:** So forex, if the rupee depreciates further then there will be a further effect. If the rupee appreciates from the present level, then it will be reversed.
- Aashish Uppanlawar:** But what is the number that has gone into the balance sheet in terms of hitting the results there or may be the goodwill increase?
- P. Ganesh:** The number that has gone to the balance sheet is a ballpark of about 175 crores. It goes by way of incremental debt. So the dollar debt when it is converted into INR, it would translate a higher INR amount.
- Aashish Uppanlawar:** On asset side, it has gone into goodwill, okay. And nothing on the gross block goes into increasing profit.
- Moderator:** Our next question is from the line of Manoj Menon from Kotak.



- Manoj Menon:** On the Household Insecticides, if you see the last four to six quarters, it has been absolutely stellar growth for Godrej consumer compared to industry growth, that's one. And probably if I may say so relatively benign competitive activity, particularly on the innovation strength from competition, so there seems to have a lot of tailwinds which seems to have gone into it. So how should I see this forward considering the fact that the lead time for innovation is fairly longer? What I am just trying to get at is that the competitive activity levels is expected to increase, remain here or go down from here?
- Adi Godrej:** We don't think competition has been benign. I think they have been very active. I think we should compliment our team which has done better than the competition and we have a strong pipeline, I mentioned about Hit Magic paper in Indonesia which is a huge new disruptive innovation, so we have a lot of pipeline in new products.
- A. Mahendran:** I want to add one more point on our innovation pipeline. If you take the last five years or 10 years, these peers you have in mind, we have been dealing with them for the last five years and we are much ahead of them consistently for the last five years on the innovation platform, particularly, Household Insecticides. So that plan is still on for the next five years also. So I don't see any issue, and as Mr. Godrej said, they are not benign, they have their own activity, but we are always ahead of them on innovation. You look at the innovation investment; also if you look at the competition, our investment was much higher there.
- Manoj Menon:** Okay, so basically can we construe that the confidence levels to significantly outperform category growth is fairly high?
- Mahesh:** Yes you can say that.
- Manoj Menon:** Okay sir, just second question on the Insecticides business. Has the Household Insecticides gross margins for the six months, kind of gone down a bit, just specifically the gross margins for the HI business in India?
- A. Mahendran:** No, it's not gone down, it's flat.
- Manoj Menon:** How about the sales mix, the coils versus the non-coils this year, this first half versus last year?



- A. Mahendran:** There is a slight shift in the mix towards the non-coil, which is marginal, not very big. Because aerosol is doing very well, and of course in liquid vaporizer segment we have reached market leadership position. So I would say the saliency of non-coil is improving definitely.
- Manoj Menon:** Sir one last question on Hair Color, if I heard Mr. Vivek Gambhir correctly little earlier commenting that it might take maybe another couple of quarters for the impact of the re-launch to be seen. I am just trying to understand from a marketing point of view that if I understand correctly, the typical replacements I think for a Hair Color from a consumer point would be a month or so. I am just trying to understand why it takes a long time for, let's say if you are looking at a market share gain or a product switching from a consumer, why it should take such a long time for that to happen?
- Adi Godrej:** Because Hair Color is an occasional use product, in a sense that you use it once a month and by the time the new product replaces the old product in the marketplace, some people still have stocks of the old product and sometimes people buy because the pack has enough for six months use. So sometime people buy a carton and not possible to shift to the new product. So we have noticed that in some of these products, it does take a while before the new product gains share. Even when we check the ACNielsen numbers, some of the old product sales are still going on, so therefore we feel that the full impact of the new advertising, new products, etc. is felt around six months after the launch.
- A. Mahendran:** Just to add to Mr. Godrej it is a grey coverage what you are talking, it depends on the age profile of the consumer that is typically a monthly one, you are right on that. But then there is a good shift happening on a lower age profile also in terms of coloring, a hair color basically. It may not be a grey coverage Vivek is saying is going to happen.
- Manoj Menon:** Sir but let's say at the industry level, what would be the black contribution, basically the dye part and the coloring part at an industry level currently?
- Adi Godrej:** Black is still the major color, but the non-black salience is growing quite considerably.
- Moderator:** Our next question is from the line of Anshul Mishra from ING Mutual Fund.



- Anshul Mishra:** My question was on the forex part, just wanted to understand these forex mark-to-market that you have done, this would be on the palm oil supply contracts that you would be having, am I right on that?
- P Ganesh:** Yes as far as standalone business is concerned, it's on palm oil.
- Anshul Mishra:** And which would flow through to the consolidated level as well?
- P Ganesh:** Yes, it flows through the consolidated aspect.
- Anshul Mishra:** When you say that your contracts till December are covered, in a way you have kind of bought dollars against it for payment in future?
- P Ganesh:** Yes, we have taken forward contracts.
- Anshul Mishra:** Yes so the January supply that will be happening in January for that you are kind of not covered and you have done a mark-to-market on it. So when in Q4, you actually take the supply and that forms part of your raw material. As and when it forms part of your raw material, suppose the dollar were to remain at Rs. 50, does that mean that at that point of time, it would form part of your raw material cost and hence the cost would be higher because of the adverse dollar movement that has already happened and you would reverse this forex mark-to-market even if dollar were to remain at 50?
- P Ganesh:** No, that's not the way it operates. The way it will actually function is that the earliest payment is in January, so for these repayments actually start from the period starting January and we have about \$22 million exposure and this is the mark-to-market impact coming out of that. So the way it will actually happen going forward is that if rupee continues to remain weak and we decide to hedge at some point before repayment or if we keep it unhedged but repay starting January and the rupee were to remain at current levels then the mark-to-market which has been taken which is notional at present gets fructified, it becomes permanent. In case the rupee depreciates further, there will be more mark-to-market impact which will become permanent. If it appreciates in the interim then part of the mark-to-market gets reversed, that's the way it will pan out.



- Anshul Mishra:** Right, so in a way what the loss that you have already taken in the P&L will get realized later on, right, which will anyways form part of your raw material cost, am I right on that, in the subsequent quarters, suppose the dollar were to remain at this level?
- P Ganesh:** This will not form part of the raw material cost because this is raw material already received and since we have credit, it's a payment which has not happened.
- Anshul Mishra:** Second question was on the dollar debt, any repayment that's going to happen in next six months on the dollar debt?
- P Ganesh:** We are covered on our repayments up to November, so the repayments falling after November are the ones which are un-hedged at the moment.
- Anshul Mishra:** November 2011?
- P Ganesh:** Yes that's right.
- Anshul Mishra:** So can you please tell us the amount of dollar repayment that could be unhedged and would fall within next six months?
- P Ganesh:** On a quarterly basis, we have typically about \$20 million of repayment.
- Anshul Mishra:** Also, I didn't quite get the part wherein you said that there is a mark-to-market on the dollar loan that has been made to other subsidiaries within the company and you said that in consol, it won't go away. I just couldn't understand that part. Why would it did not go away in the consol that mark-to-market?
- P Ganesh:** These are dollar loans given by a holding company to its subsidiary company, and this is the actual transaction which has happened at the operating company level, say in Latin America as well as Indonesia and therefore for these entities it's a dollar debt which needs to be paid. So it's a repayment obligation when those currencies have also depreciated against the dollar, there is a mark-to-market impact.
- Anshul Mishra:** Mark-to-market impact is there on the subsidiary but then when they make the repayment you gain at the holding company level because of that repayment because you get more, does that not work that way?



- P Ganesh:** The holding company which has given the loan has its functional currency as dollar. That's the reason why this will remain over that, but again, if the currencies appreciate against the dollar, this gets reversed. And these are very long-term shareholder loans, so in that sense it becomes purely notional.
- Anshul Mishra:** One last question, this is on the business front about the synergy benefits between GHPL and GCPL. Just wanted to understand is the cross pollination kind of over, in a sense that where you had Soaps, the Insecticides have reached and where you had Insecticides, Soaps have reached, is that thing over pan India or one can expect probably in coming quarters, some additional cross pollination to happen?
- A.Mahendran:** It is a process which has just started, I would say the benefits we have started getting for the last two quarters and it will continue for the next two quarters or even more.
- Adi Godrej:** So basically the answer is more benefits will start accruing over the next few quarters and all the benefits will be cumulatively continued for almost all time.
- Moderator:** We have a question from the line of Varun Lohchab from Religare Capital Markets.
- Varun Lohchab:** Sir, my question was on the organic growth in Africa. If you could just let us know the revenue and EBITDA numbers for the Darling group that you have booked in this quarter?
- P Ganesh:** It's not a very large number as far as Darling group is concerned and therefore looking at Q3 would be the right way of looking at Darling.
- Varun Lohchab:** So in this quarter in terms of revenue will it be like 30-40 crore to that extent or even lower than that?
- P Ganesh:** No, it's not a significant number.
- Varun Lohchab:** Okay, and secondly in terms of the ROE profile of the international business, given the margins are quite low in Latin America for the reasons you said and even Keyline margins are low, what would be the ROE profile of your international business and where you see that going forward?
- P Ganesh:** Country to country it varies and clearly when we look at the balance sheet of each of the companies, the only major capital essentially is actually working capital and with a mix of



increase in profits as we go along as well as optimization of capital employed in each of the businesses, we would expect Return on Equity to improve on existing businesses as we go along.

Adi Godrej: As you can see all our international businesses are accretive. If you see the difference between the consolidated profits and the domestic profits is quite high and that is after deducting the cost of acquisition and the interest cost of acquisition, so they are all accretive.

Varun Lohchab: Sir just on that question, will they be EVA accretive, even if you take the mark-to-market on the debt side, like given the current rupee depreciation

Adi Godrej: That's difficult to tell because the mark-to-market has just started in this quarter, so we expect very strong EVA accretiveness, but that is over a period of time.

Varun Lohchab: So would they be EVA accretive, if they were equity funded?

Adi Godrej: EVA accretiveness will depend on a period of time. We expect all of them to be very strongly EVA accretive. The valuation of the acquisition also keeps increasing.

Varun Lohchab: And sir if they were say funded by the cost of equity of the Indian business then would they still be EVA accretive?

Adi Godrej: Yes, that is why we invest in them because we expect them to be extremely EVA accretive, and you must remember that when you acquire a company, not only do you take in the profits the company makes, but the valuation of the company keeps increasing as time goes by, so there is tremendous valuation. So we did a number on our Rapidol acquisition and we think it would be worth at least five times what we paid for it about 4.5 years ago.

Moderator: Thank you so much. I would now like to hand the call over to Mr. Pritesh Chheda from Emkay global for closing comments.

Pritesh Chheda: On behalf of Emkay I would once again like to thank you all for joining the call. We thank the management for giving us the opportunity to host the call. We wish them good luck and a very happy Diwali and great New Year ahead. Over to you Mr. Adi Godrej, for closing comments.



Adi Godrej:

Thank you Pritesh. It was good talking to all of you. I would like to add my very good wishes for a happy Diwali and a very successful and prosperous New Year to all. Thank you.

Moderator:

Thank you so much. On behalf of Emkay Global Financial Services, that concludes this conference. Thank you for joining us. You may now disconnect your lines.